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SUBJECT: G-20 LEADERS SUMMIT: LATEST AUSTRALIAN VIEWS FROM  
NEWLY APPOINTED SPECIAL ENVOY

REF: A. CANBERRA 1096

[1](#)B. CANBERRA 1076

Classified By: Economic Counselor Edgard Kagan for reasons 1.4 (b/d).

Summary

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[1](#)1. (C/NF) Australian thinking about the goals for the upcoming G-20 leaders summit has evolved, according to newly-appointed Prime Minister's Special Envoy for the International Economy Mike Callaghan. Callaghan was about to leave later in the day for China, the UK and the United States. Sharing the latest draft of Australia's goals paper for the Summit, Callaghan said Australia now believes that the Summit should create three vice two working groups, with the third group addressing efforts to stimulate growth (the first would address short-term stabilization of financial markets and the second would look at longer term reforms). The goal of the financial stabilization and economic growth working groups would be to do real-time coordination between countries to minimize the risk of unintended consequences resulting from actions by different countries. It will also be important to get countries to think through how they will wind down their interventions in financial markets and to coordinate these efforts. "The last thing we want are new institutions," said Callaghan, stressing that the goal of the Summit should be to make sure that existing systems work. Noting high expectations for the Summit in Australia and around the world, Callaghan stressed the importance of concrete results. The draft we were given suggested that the long-term reform working group could be chaired by the UK and Australia. Following the discussion, Callaghan sent us a new version suggesting the working group be chaired by the UK, Korea and "perhaps a third country." Callaghan commented that Australia has been hearing about the possibility of a

follow-up G-20 Leaders Summit being held by mid-January. He said Australia supports aggressive efforts to make progress on stabilizing financial markets but wonders if this might be an unrealistically early date. End Summary.

#### New Special Envoy

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¶2. (C/NF) Prime Minister Kevin Rudd has appointed Mike Callaghan as his Special Envoy on the International Economy. A long-time Treasury official who served as IMF Executive Director representing Australia and 13 other countries from 2002-2004, Callaghan was most recently a Deputy Secretary at the Department of Environment, Water, Heritage and the Arts after having served as a Deputy Secretary for the Revenue Group at the Treasury. Callaghan served as Chief of Staff to former Treasurer Peter Costello from 1999-2000 and was the former Treasurer Peter Costello from 1999-2000 and was the senior Treasury representative involved with the reform of Australia's financial regulatory structures in the late-1990s. Callaghan played an active role in Australia's chairing of the G-20 in 2006.

#### Upcoming Travel to China, UK and United States

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¶3. (C/NF) Callaghan said Australia wants to support U.S. efforts to address the global financial crisis during an October 30 meeting with Econcouns to preview his upcoming travel to China, the UK and the United States. Callaghan was planning to leave later October 30 for Beijing. He does not know what to expect in Beijing but believes China is increasingly concerned about Asian financial market stability. Callaghan is looking forward to his Washington meetings and understands that meetings have been set up with Deputy National Security Advisor Price, Treasury Under Secretary McCormick and Under Secretary Jeffery.

#### Further on Aussie Thinking

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¶4. (C/NF) Australia has further refined its thinking on the Summit. Callaghan provided a new version of the internal working draft of Australia's goals paper for the Summit (original version reported Canberra 1096), which he said largely fleshed out the earlier ideas. The one major change is that Australia now would like to see creation of three vice two working groups. Arguing the importance of coordinating the efforts to stimulate economic growth that are taking place in every G-20 country, Callaghan said it is unrealistic to expect one working group to do this and address financial market stabilization. Australia now believes that the working group on financial market stabilization should be jointly chaired by the United States and Brazil. This would highlight the role of developing countries and give them "buy in" to the process, according to Callaghan. It would also push back against the notion that financial market turmoil is a problem of developed and not developing countries. The role of this working group should be to facilitate coordination of government actions to stabilize financial markets as well as the unwinding of these steps once markets have stabilized.

¶5. (C/NF) The working group on stimulating economic growth could be chaired by Germany and China, Callaghan suggested. Germany will be very important to generating growth within the Eurozone, while China will be viewed as the logical leader amongst developing countries, he said. Noting that France will push hard for a leading role, Callaghan said Australia sees Germany as far preferable and will support opposition to the French.

¶6. (C/NF) Callaghan said that Australian thinking about the working group on longer term reform had also evolved. Canberra still sees this group as trying to improve existing systems rather than create new structures. However, the Aussies now believe that they should be the co-chairs, along with the UK, of this group. Econcouns pointed out that this

Qwith the UK, of this group. Econcouns pointed out that this undermines the original argument that the UK and Korea should co-chair such a working group in their capacities as the current and incoming chairs of the G-20. Econcouns also noted unhappiness with recent Australian actions involving the summit and suggested that pushing a leading Aussie role might not go over well. Callaghan took the point and followed up an hour after the meeting with a new draft referring to the UK, Korea and "perhaps another country" serving as co-chairs. Callaghan also said that Australia will probably be ready to provide resources to support this working group in the form of staff as well possible support for participation by other countries.

#### No New Institutions, but Better Coordination

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17. (C/NF) Stressing that Australia does not want new institutions, Callaghan said that recent events have highlighted for Canberra the importance of coordinating international moves. Noting the continuing brouhaha over various investment funds freezing withdrawals from over A\$25 billion (\$15 billion) worth of funds (reftel B), Callaghan said this was the unintended consequence of the Government's decision to guarantee all banking deposits. That decision led investors in mortgage funds and other investment vehicles to try to move their money to banks that were covered by the guarantee, which in turn forced the funds to freeze withdrawals. The decision to offer the unlimited guarantees was not driven by problems in Australia's banks, as the four major banks that control 80% of the market are all among the world's 12 remaining AAA-rated institutions. According to Callaghan, the decision was driven by the need to ensure that the Australian banks remained competitive with banks in other OECD countries that were being covered by deposit guarantees.

Better international coordination might have given more time for Australia to come up with a better policy approach. The same will almost certainly be true as such measures are unwound, Callaghan said.

#### Followup Summit?

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18. (C/NF) Callaghan commented that Australia has been hearing about the possibility of a follow-up G-20 Leaders Summit being held by mid-January. He said Australia supports aggressive efforts to make progress on stabilizing financial markets but wonders if this might be an unrealistically early date.

#### Latest Australian Draft

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19. (C/NF) Australian Internal Working Draft of G-20 Leaders Summit Goals Paper. Begin Text:

#### G-20 Leaders Summit

The summit should provide a high-level strategic assessment of the way forward, as well as providing the political impetus for advancing the necessary changes. The objectives for the Leaders Summit could be investigated around three broad timeframes.

##### (i) Immediate considerations

- stabilization of financial markets;
- bedding down measures to restore market confidence;
- impact on emerging markets and developed economics, including, adequacy of financing and support arrangements; and
- coordinated efforts to stimulate economic growth.

##### (ii) Transition issues

- coordinated and orderly withdrawal of the

measures taken to restore confidence in financial markets; and

- renewed actions to prevent the build up of protectionism.

(iii) Longer-term objectives

- identifying and implementing the measures needed to strengthen financial and economic markets and reduce the likelihood of future crisis.

In light of the fact that many countries are working quickly to bed down regulatory changes within their respective national economics, there are likely to be practical difficulties if leaders were to try to establish too many working groups simultaneously.

To overcome this obstacle, leaders could commission three working groups.

- The more immediate and pressing issues would be undertaken by a working group (possibly to be chaired by the US and Brazil) that would work informally and report frequently to coordinate real-time advice back to all G-20 members to ensure that:

- confidence is restored and maintained such that banks and financial institutions continue to lend to households and businesses.

- all available tools are being deployed to support systemically important financial institutions;

- international cooperation in the implementation of the measures introduced to restore market confidence, such as deposit insurance, guarantee arrangements and government capital injections into financial institutions, and there is ongoing close global coordination when such measures are unwound;

- G 20 members are leading by example in implementing the FSF recommendations for strengthening financial systems;

- effective and efficient arrangements are in place, particularly through the International Financial Institutions, to meet the financing and adjustment requirements of emerging markets impacted by the crisis. This would include monitoring the responsiveness of the IFI,s as well as the adequacy of their resource base.

A second working group (possibly chaired by China and Germany) would focus on ensuring that all available measures are being taken to minimize the impact of the financial crisis on activity and that economic growth is restored.

Looking further ahead, a third working group (perhaps chaired by the UK, Korea and perhaps another country, and drawing on secondments from G-20 members) would begin work on the longer-term objective of developing an action plan to strengthen the regulatory structure for financial markets and institutions in an increasingly integrated global economy. The objective of this working group would be to provide the impetus for the establishment of globally accepted standards of supervision and regulation of financial markets and institutions which would be applied equally and consistently by all countries. In undertaking this task the working group would consider:

- ensuring that systemically important financial institutions are appropriately regulated with full disclosure of balance sheet and off-balance sheet exposures, recognizing that systemically important institutions can vary over time and between countries

- assessing whether the regulation and supervision of financial institutions should be based more on the type of financial activity being undertaken and less on the type of intermediary

- establishing supervisory systems that are not pro-cyclical, including strengthening banks capital positions in the good times as a buffer for the bad times, implementing sound loan-loss provisioning, and developing accounting rules to evaluate risk that take a more medium-term perspective and do not encourage institutions to think that risk is low just because asset prices are high, or recent asset price volatility has been low
- ensuring financial institutions have clear internal incentives to promote financial stability, including through regulators setting higher capital requirements for banks with executive compensation arrangements which reward short-term returns or excessive risk taking.
- establishing regulatory frameworks such that central banks have the overall responsibility for the stability of the financial system and that they have the capability to perform this role
- developing effective early warning systems that better understand the interaction between macro-financial and systemic risks and ensuring that there are mechanisms to respond to identified risks
- introducing mechanisms for more effective cross-border supervision of global firms and better mechanisms for cooperation in a crisis
- enhanced cooperation between international standards setters, like the FSF, and the International Financial Institutions, particularly the IMF and World Bank.

An interim report on reform priorities could be presented to a special G-20 finance ministers meeting ahead of the IMF/World Bank meetings in April, with a final report presented to leaders in the second half of 2009.

End Text.

McCallum